

Before the
UNITED STATES
SECURITIES EXCHANGE COMMISSION

PETITION TO SET ASIDE
ADMINISTRATIVE PROCEEDINGS 3-9599

Brought By
JOHN GARDNER BLACK, (“Petitioner”)
DEVON CAPITAL MANAGEMENT

I. Introduction

Petitioner John Gardner Black and his company, Devon Capital Management (“Devon”), respectfully request that the Securities Exchange Commission [“SEC” or “Commission”] set aside its May 4, 1999 “ORDER INSTITUTING PUBLIC PROCEEDINGS [*sic*], MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS”, [“Order”]. The factual basis for the proceedings no longer constitutes violations of Sections 206(1), 206(2) or 206(4) of the Investment Advisors Act of 1940. Further, the factual basis no longer supports the claim of violations of Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Act of 1934 and Rule 10b-5 promulgated thereunder. As delineated in the Financial Accounting Standards Board [“FASB”] interpretation of Rule 157 as of April 2, 2009, published April 7, 2009, as well as the Commission’s statements and representations to Congress of December 30, 2008, the valuation procedures employed by Black and Devon are required for reporting and

regulated entities effective March 15, 2009. In addition, the valuation method advanced by the Commission in its *ex parte* complaint filed September 26, 1997, is a method specifically precluded by the FASB's staff interpretation of FASB Rule 157.

II. The Collateralized Investment Agreement ("CIA")

On April 27, 2001, the Commission filed a brief in US District Court for the Western District of Pennsylvania in which it stated that the contract between Financial Management Sciences ("FMS") and the clients of Devon was a security, specifically an investment contract, defined as: "(1) an investment of money; (2) in a common enterprise; and, (3) with a reasonable expectation of profits to be generated by the managerial or entrepreneurial efforts of others." On May 9, 2001 the district court issued its opinion holding that the CIA was an investment contract security.

Neither in the Commission's April 27, 2001 brief, nor in the Commission's September 26, 1997 complaint, nor in the Commission's May 4, 1999 Order is the value of the CIA claimed or alleged to have been misrepresented in monthly statements. Additionally, the US Attorney's office filed a brief in district court on September 30, 2003 in which it stated that the CIA was "...not susceptible to independent evaluation", implying that a valuation was never done or if done, the results were never released publicly nor to Petitioner.

On December 13, 2005, the District Court issued an order in which it stated that it had "litigated and resolved" the market value of the CIA. Neither Petitioner nor his companies were represented in that litigation. However, it is reasonable to presume that the party who represented the interests of the corporations would have argued that the CIAs were worth the value reflected in monthly statements, based upon a reasonable expectation of the present value profits to be derived from **all** the investments owned by FMS.

It can be further presumed that the Commission's argument of valuation remained unchanged from its September 26, 1997 complaint. Specifically, the Commission chose to ignore company specific information, i.e., an estimated \$75 million of reasonably expected profits on the remaining investments owned by FMS, that was not used by the Commission to support the valuation of the CIAs or any other investment owned by FMS.

In analyzing the value of the CIA for monthly statements, Petitioner and his companies determined the fair value predicated upon a reasonable expectation of profits derived through the efforts of others and company specific information available to management. That fair value of the CIA was reported monthly to clients. A fair and accurate report of a security's fair value is not a violation of Sections 206(1), 206(2) or 206(4) of the Investment Advisors Act of 1940. An "offer, purchase or sale" of a security at fair value is not a violation of Section 17(a) of the Securities Act of 1933, Section 10(b) of the Securities Act of 1934 and Rule 10b-5 promulgated thereunder.

III. The Valuation of Investments Owned by FMS

On August 29, 1997, the SEC completed a three day audit of Devon and FMS. Management gave to the Commission's auditors a present value analysis of the investments owned by FMS, prepared pursuant to the Internal Revenue Service's Arbitrage Regulations, 26 CFR § 1.148-5. [The valuation of investments under the arbitrage regulations is very similar to the method required pursuant to FASB 157.] The valuation of the Collateralized Mortgage Obligation ("CMO"), CUSIP No. 31359EEN7, purchased in January of 1996, was conducted pursuant to those regulations. That CMO last traded in the market twenty months before the Commission filed its complaint. Specifically, the reasonably expected cash flows from the entire portfolio were amalgamated and discounted to present value at prevailing market rates. Company

specific information, the surplus earnings on all investments, was included in the valuation of the CMO.

The above documents were in the possession of the SEC on August 29, 1997 and the US Attorney's Office for the Western District of Pennsylvania as well as the trustee, Richard Thornburg, on September 26, 1997.

On September 26, 1997, following several *ex parte* judicial proceedings, the SEC introduced its complaint in district court for the Western District of Pennsylvania. The complaint alleged that Petitioner had not valued the CMO at its forced liquidation value, which the Commission obtained solely from Lehman Brothers, even though the CMO had not traded in over a year and a half. Further, Lehman's valuation did not incorporate company specific information, such as the surplus valuation on the remaining investments. No other valuation was obtained from any other legitimate bidder.

IV. Currently Required Valuation Procedures

On December 30, 2008, the SEC supplied to the United States Congress a report in which it held that "Company-specific information should be factored into fair value measurement when relevant information is not observable in the market." In the matter of Devon, the Commission did not incorporate all company specific information when valuing the CMO. Had the Commission used the current fair value methods now required, the fair value of the CMO, derived using present value analysis would have supported the valuation supplied to clients in monthly statements. The current regulations delineate an identical method to the one employed by Petitioner in representing the fair value of both the CIA and the CMO to clients.

On April 2, 2009 the Financial Accounting Standards Board [“FASB”] issued and approved revisions to FASB Rule 157. The revisions are consistent with the Commission’s December 30, 2008 report to the US Congress. In determining the value of an inactively traded security such as the CMO, management is to presume a period of time for marketing the security which includes divulging all relevant company specific information as well as a solicitation of value from multiple bidders. The fair value of the security is to be derived by discounting to present value expected cash flows on that security plus any company specific information such as surplus valuation from other securities. This is exactly the procedure used by Petitioner and supports his valuation of the CMO.

V. Summary

On September 26, 1997 the Commission filed its complaint against Black, Devon and FMS. On May 4, 1999 the Commission issued its order imposing an industry bar of indefinite duration against Black and revoking the Investment Advisor registration of Devon.

Effective April 2, 2009, supported by the Commission’s report to Congress of December 30, 2008, the operating procedures followed by Petitioner and his companies are now required by the Commission for all reporting entities.

Accordingly, there can no longer be a public purpose nor in the public’s interest to continue to enforce the orders of May 4, 1999. Petitioner respectfully requests that those orders be set aside.

May 26, 2009

Respectfully Submitted,

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